POSITION PAPER

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Reforming the Structure of the EU Banking Sector

HIGH-LEVEL EXPERT GROUP

Introduction

The new European System of Financial Supervision will significantly improve cross-border oversight and should contribute to greater financial stability. Improved capital and liquidity measures will build a more resilient banking sector and improve the banking sector's ability to absorb shocks arising from financial and economic stress.

Clear criteria for early cross-border interventions, common burden-sharing and effective resolution regimes are a vital complement to these proposals. A credible framework for winding down banks, if properly done, would help curb excessive risk-taking through greater market discipline, provide better protection for shareholders, significantly reduce the likelihood of calls on public funds, and limit the need for heavy-handed regulation. Private sector solutions to mitigate risk and make banks' management, shareholders and creditors more accountable will be key to a balanced agenda for financial market reforms.

Consistency in cross-border arrangements will be particularly important to preserve market integration. The risks involved in segmenting financial services along national borders should not be underestimated, and would have severe consequences for the functioning of the European internal market and its growth potential.

Businesses Needs

European businesses, and especially the smaller and medium-sized businesses, depend highly on bank lending (the European banks' share of credit intermediation is 3 times higher than in the US and small businesses borrow 2 times more from banks than large corporations). These companies need the availability of financing from the international banks that are active in the EU. These banks provide liquidity to the financial markets and are active in specialist financing and business niches. They need to be healthy to support EU business and the broader economy.

Companies benefit from banking with large and diverse banks. They often need the balance sheet of a large bank to support them, for example in the case of large infrastructure projects or when a debt or equity capital issuance has to be underwritten. Large and diverse banks have more flexibility to use their balance sheets, using funding across customer groups and from a diverse range of sources which permits more extensive lending activity.

Companies are exposed to different risks and face different challenges depending on their size, activities and the economic cycle. Universal banks are able to manage these risks by being able to diversify them across a wide group of different customers.

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Companies use a wide variety of banking products. Typically, smaller businesses use a narrower range of products but as soon as a business starts to grow, and becomes more international and complex, it needs more sophisticated products which it may not always be able to obtain from large investment banks. Not only does it need to invest and finance its business but also to manage its interest, foreign exchange and commodity risk. Although it is common for companies to use several banks, it is often more efficient, especially for growing and small and medium-sized companies, to source integrated services from a bank with which they have a long standing relationship and which understands the needs of the company concerned. Such an institution can make quick, qualitative judgements about the credit quality of the company concerned. If a single bank can provide such a wide range of banking products, it can also reduce complexity and therefore the operational risk of the company concerned.

Businesses can also obtain cost efficiencies from using a single bank and cost efficiencies for large banks can be passed on to businesses reducing the costs overall. They can negotiate better contracts and it is easier to manage and monitor a relationship with a single bank. Businesses also often net exposures related to financial instruments used to manage risk with one bank to reduce its credit positions, credit risk and funding requirements.

Conclusion

BUSINESSEUROPE sees benefits in the integrated services that are provided by large universal banks. Having said this, BUSINESSEUROPE believes that enhanced competition will increase transparency in the pricing of bank products and services.

The EU should therefore focus on measures that reduce barriers to entry into the banking market. This will encourage more diverse forms of finance - including non-bank finance - and ensure that the EU remains an attractive market increasing the choice and possibilities for businesses to access the finance they need to create growth and jobs.

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